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In the Supreme Court of the United States

OCTOBER TERM, 1995

D. GRANT PEACOCK, *Petitioner*

v.

JACK L. THOMAS, *Respondent*

On Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF OF THE NATIONAL ASSOCIATION OF REAL ESTATE INVESTMENT MANAGERS AS AMICUS CURIAE IN SUPPORT OF PETITIONER

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36 pp

QUESTIONS PRESENTED

1. Whether a federal court has ancillary jurisdiction to adjudicate a plaintiff's factually unrelated claim to enforce a prior judgment against a non-party to the original action.

2. Whether it is consistent with the statutory scheme of the Employee Retirement Income Security Act ("ERISA") to impose personal liability on a nonfiduciary by piercing the corporate veil of a fiduciary.

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BRIEF OF THE NATIONAL ASSOCIATION OF REAL ESTATE INVESTMENT MANAGERS AS AMICUS CURIAE IN SUPPORT OF PETITIONER

INTEREST OF THE AMICUS CURIAE

The National Association of Real Estate Investment Managers ("NAREIM") is an association of approximately 60 firms that manage large, equity-oriented real estate investments or act as investment and asset managers to various institutional holders of such real estate. Because ERISA pension plans are major investors in real estate,

NAREIM member firms often serve as investment manager fiduciaries of these plans. As a result, they have a strong interest in ensuring that any duties or liabilities imposed under ERISA with respect to such activities are consistent with the language of the statute and predictable in application. Specifically, shareholders (both corporate and individual) of real estate investment managers are ERISA fiduciaries only when they expressly assume that obligation or function as fiduciaries. Nonfiduciary shareholders thus have a substantial concern about being saddled with ERISA liability based on their corporate ownership rather than the established tests of fiduciary status.[1]

SUMMARY OF ARGUMENT

Respondent's veil-piercing action cannot proceed against petitioner for two independent reasons. First, this case does not fall within the ancillary jurisdiction of the federal courts. Adjudication of petitioner's liability is not necessary to vindicate the federal court's authority or to effectuate its decrees. There has been no allegation that anyone bound by the original judgment has flouted or failed to comply with that judgment. Rather, this "ancillary" action resulted in a completely *different* judgment against a *different* party premised on *different* facts and a *different* legal theory. This Court's controlling precedent precludes the assertion of ancillary jurisdiction when a judgment creditor seeks to require a nondiverse third party to pay the judgment. *H.C. Cook Co.* v. *Beecher*, 217 U.S. 497 (1910).

The action to impose liability on petitioner also lacks factual interdependence with the fiduciary action that preceded it. Determining the issue of fiduciary liability required an inquiry into whether petitioner or others exercised

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[1] The parties' letters of consent to the filing of this brief have been filed with the Clerk pursuant to Rule 37.3 of the Rules of this Court.

discretionary authority and control over the management and administration of fund assets. By contrast, the veil-piercing action required an inquiry into a shareholder's dominance of his corporation and observation of the corporate form; indeed, it focused on conduct that occurred *after* the original judgment.

Second, even if ancillary jurisdiction exists, the Fourth Circuit's theory of implied liability is inconsistent with the explicit and careful distinctions in ERISA between the duties of those who are fiduciaries under the statute and those who are not. These distinctions have very significant practical implications. ERISA fiduciaries are subject to a stringent standard of care for their own conduct. Fiduciaries also can be held liable for acts and omissions of cofiduciaries as well as for violations of ERISA's prophylactic and highly technical prohibited transaction rules. These obligations cannot be contracted away even if the fiduciary acts in good faith and in the best interest of the plan and its participants and beneficiaries. The Fourth Circuit's expansion of the scope of such liability to the shareholders of fiduciaries undercuts ERISA's fundamental distinctions between fiduciaries and nonfiduciaries and is likely to increase materially the cost to investment managers of doing business.

In imposing ERISA liability on petitioner, a nonfiduciary, the Fourth Circuit did not purport to find either a specific cause of action or a specific source of authority of nonfiduciary duty under the statute, for there is none. It simply borrowed a liberal veil-piercing rule adopted in the totally different context of regulating the obligations of employers under ERISA. As this Court only recently held, however, there is a strong presumption against federal courts creating new causes of action or remedies within the ERISA statutory scheme. *Mertens* v. *Hewitt Associates*, 113 S. Ct. 2063, 2067 (1993).

The Fourth Circuit offered essentially no rationale for overcoming that presumption. In fact, allowing the action

created here would upset the delicate balance of competing interests legislated by Congress; it would render ERISA liabilities wholly unpredictable; and it would ignore statutory language showing that Congress has already regulated the relationship among plans, fiduciaries and their shareholders. Finally, there is a fundamental inconsistency between ERISA's functional definition of fiduciary status and corporate veil-piercing when used to impose liability on a nonfiduciary.

ARGUMENT

I. ANCILLARY JURISDICTION DOES NOT ENCOMPASS A PLAINTIFF'S UNRELATED POST-JUDGMENT CLAIMS AGAINST THIRD PARTIES

The Fourth Circuit's jurisdictional ruling vastly expands the scope of ancillary jurisdiction to include new and different claims, brought after the original action, involving parties and facts different from the original action. Ancillary jurisdiction, as it has been framed by this Court, does not reach so far.

This Court has identified two purposes served by the ancillary jurisdiction of the federal courts: (1) to permit disposition by a single court of claims that are factually interdependent; and (2) to enable a court to manage its proceedings, vindicate its authority, and effectuate its decrees. *Kokkonen* v. *Guardian Life Ins. Co. of America*, 114 S. Ct. 1673, 1676 (1994). Neither circumstance exists here.

A. The Expansion Of The Federal Court's Limited Jurisdiction Permitted Below Is Unnecessary To Enable The Court To Vindicate Its Authority

The Fourth Circuit did not hold that ancillary jurisdiction was necessary to vindicate the federal court's authority. The assertion of jurisdiction was not designed to enforce the judgment of a federal court. Rather, it was designed to enter

a new judgment holding a third party responsible for the liabilities imposed by the original judgment.

To be sure, federal courts have broad authority to enforce their judgments. See *Riggs* v. *Johnson County*, 73 U.S. 166, 187 (1867); *Bank of the United States* v. *Halstead*, 23 U.S. (10 Wheat.) 51 (1825). For example, federal courts have unquestioned jurisdiction to issue orders forcing a party to carry out the terms of the court's judgment. See, *e.g.*, *Dugas* v. *American Surety Co.*, 300 U.S. 414, 428 (1937); *Supreme Tribe of Ben-Hur* v. *Cauble*, 255 U.S. 356, 367 (1921); *Root* v. *Woolworth*, 150 U.S. 401, 410-413 (1893). The enforcement proceeding enables the court to ensure that its rulings are given effect and that the parties bound by the judgment comply with it. See *id.* at 410-412.

The holdings of this Court make clear, however, that federal jurisdiction to enforce judgments in supplemental proceedings is not unlimited. *Kokkonen*, 114 S. Ct. at 1676-1677. Specifically, this Court has never held that jurisdiction exists to allow a plaintiff in a subsequent action to bring a claim that requests relief of a "different kind" or that rests on a "different principle." *Dugas*, 300 U.S. at 428; see, *e.g.*, *Beecher*, 217 U.S. at 499; *Hale* v. *Allinson*, 188 U.S. 56, 81 (1903). In fact, the Court has expressly rejected as "expansive" dicta the notion that a federal court has jurisdiction to provide precisely the kind of relief respondent seeks here. In *Kokkonen*, the Court declined to endorse a definition of ancillary jurisdiction as

> "[a] bill filed to continue a former litigation in the same court . . . to obtain and secure the fruits, benefits and advantages of the proceedings and judgment in a former suit in the same court by the same or additional parties . . . or to obtain any equitable relief in regard to, or connected with, or growing out of, any judgment or proceeding at law rendered in the same court * * *."

114 S. Ct. at 1676 (quoting *Julian* v. *Central Trust Co.*, 193 U.S. 93, 113-114 (1904)).

The Fourth Circuit acknowledged that federal courts do not have jurisdiction over "independent" enforcement actions. Pet. App. 15a.[2] The court of appeals concluded, however, that respondent's veil-piercing action was *not* independent, because the action was a derivative claim that attempted to determine whether petitioner, a corporate shareholder, could be held liable for a pre-existing judgment entered against the corporation. *Id.* at 13a. The court reasoned that

> [b]ecause identification of those parties who are liable is necessarily antecedent to procedural enforcement of the judgment against those parties, and because *Riggs* establishes that federal courts have "ancillary" jurisdiction over enforcement of judgments, it would seem that the federal courts' "ancillary" jurisdiction would extend to the instant attempt to pierce the corporate veil.

Ibid. This reasoning plainly misconceives the breadth of ancillary jurisdiction and cannot be reconciled with this Court's decision in *H.C. Cook Co.* v. *Beecher*, 217 U.S. 497 (1910).

Beecher involved a suit by a judgment creditor of a corporation found liable for patent infringement who, unable to collect against the corporation, sued its directors. The judgment creditor alleged that the directors took actions during the pendency of the patent infringement proceeding to render the corporation insolvent in the event an adverse judgment was entered. After emphasizing that the second action did not deal with the patent but only the existence of the judgment, the Court flatly disagreed with the contention

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[2] It is undisputed that there is no diversity of citizenship and no basis for federal question jurisdiction here other than the fact that the suit seeks to enforce a judgment obtained pursuant to ERISA. Pet. App. 11a n.6.

that the action was "ancillary" to the judgment in the former suit, "which, of course, it is not." 217 U.S. at 498-499. The Court held that "if the directors are under obligations by Connecticut law to pay a judgment against their corporation, that is not a matter that can be litigated between citizens of the same state, in the [federal courts]." *Id.* at 499. Indeed, *Beecher* was a more compelling case for the exercise of ancillary federal jurisdiction, because the plaintiff charged that the defendants' activities, which occurred while the patent suit was being litigated, were intended to frustrate the effect of the federal judgment.

This Court has never departed from or questioned the holding of *Beecher*, and there is no reason for it to do so now. Indeed, the Court's recent decision in *Kokkonen* demonstrates the continuing vitality of the principles enunciated in *Beecher*. See 114 S. Ct. at 1676. Simply stated, ancillary jurisdiction, as framed by *Beecher* and *Kokkonen*, does not enable a federal court to entertain every subsequent action by a plaintiff to identify an individual or entity against whom an existing judgment might be satisfied. Rather, a federal court lacks ancillary jurisdiction to hear a claim where the plaintiff seeks a different kind of substantive relief. *Beecher* involved the question — not at issue in the original action — whether corporate shareholders were under a state-law obligation to pay a patent judgment already obtained against their corporation. This case involves the question — also not at issue in the original action — whether a controlling shareholder has an obligation to satisfy an ERISA judgment already obtained against his corporation. *Beecher* clearly held that the federal courts lack jurisdiction to hear this kind of ancillary claim. 217 U.S. at 497.

The Fourth Circuit sought to avoid the holding in *Beecher* in two ways, neither of which is persuasive. First, although the court of appeals observed that "the doctrine of piercing the corporate veil is not a mere procedural rule relating to 'how' a judgment is to be enforced, but is, rather,

a substantive rule of liability" (Pet. App. 12a), it ignored the obvious implication of this observation — that respondent was attempting to secure a different kind of relief. Instead, the court reasoned that any effort by a plaintiff to satisfy a prior federal judgment fell within the federal court's jurisdiction because it was "necessarily antecedent" to procedural enforcement of the judgment. *Id.* at 13a. This reasoning ignores the fact that "[a] distinction must be drawn between those acts which are necessary to enforce a judgment or order and those which are done merely for the sake of procedural convenience and bear no relationship to the court's earlier exercise of constitutional or statutory jurisdiction." *Eagerton* v. *Valuations, Inc.*, 698 F.2d 1115, 1119 (11th Cir. 1983). The Fourth Circuit's rationale would allow a claimant to use the federal courts to pursue anyone against whom an insolvent fiduciary might have a claim as "necessarily antecedent" to enforcing the federal judgment.[3]

The wrong alleged in this case is not one that imperils the operation of the federal court. See *Kokkonen*, 114 S. Ct. at 1676. In *Kokkonen*, the Court noted that "the only order here was that the suit be dismissed, a disposition that is in no way flouted or imperiled by the alleged breach of the settlement agreement." *Id.* at 1677. Similarly, here the federal court's order was that Tru-Tech, Inc. ("Tru-Tech") was liable to respondent under ERISA and that petitioner was *not* liable, an order that is neither flouted nor imperiled by petitioner's unwillingness to assume the debts of Tru-Tech.

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[3] That petitioner was a party to the original proceeding is of no significance. The courts have held that a party found not liable in the original action should be considered a non-party in a subsequent enforcement action. *Argento* v. *Village of Melrose Park*, 838 F.2d 1483, 1488 n.7 (7th Cir. 1988); *Skevofilax* v. *Quigley*, 810 F.2d 378, 384 (3d Cir. 1987) (en banc), cert. denied, 481 U.S. 1029 (1987); *Berry* v. *McLemore*, 795 F.2d 452, 455 n.2 (5th Cir. 1986).

Indeed, it is perfectly consistent with the federal court's judgment that petitioner has no obligation to respondent under ERISA.

Just as the *Kokkonen* plaintiff asserted a purely state law claim, so does respondent. If, as respondent argues, petitioner improperly stripped Tru-Tech of its assets before the judgment could be satisfied, his remedy is a state court action to void the fraudulent transfers or pierce the corporate veil. Such an action would require the court to resolve new and different factual issues between new parties. Federal courts do not have the power to entertain such efforts. As *Beecher* makes clear, a plaintiff who brings a veil-piercing claim against a controlling shareholder is not attempting to enforce the federal judgment received against the corporation; rather, he is using the federal judgment to create new state law liabilities against a stranger to the federal judgment.

Second, the Fourth Circuit asserted that "*Beecher* is factually distinguishable from the case at bar." Pet. App. 15a. The court of appeals stated that "the instant case involves allegations that [petitioner] deliberately engaged in improper transfers and improperly ignored corporate formalities with the specific purpose of evading the already-extent [sic] judgment against Tru-Tech, [while] *Beecher* involved an allegation that corporate directors, acting within their legal capacity, voted to continue sales of a product which was the subject of a then-pending patent infringement suit." *Ibid.* We submit that the jurisdictional power of the federal courts to adjudicate substantively different claims in enforcement actions cannot rest on so slender a factual distinction. As just discussed, the question instead turns on whether the plaintiff is merely attempting to execute the prior judgment, or whether the plaintiff is attempting to impose liability on new parties on the basis of new grounds that involve the litigation of new and different questions. That is unquestionably the case here.

B. The Veil-Piercing Action Lacks The Factual Interdependence With The ERISA Action To Support Ancillary Jurisdiction

An exercise of ancillary jurisdiction also is inappropriate here because the underlying ERISA action and the subsequent veil-piercing action involve altogether different factual issues. The ERISA action involved the question whether Tru-Tech complied with its fiduciary duty in administering an ERISA plan. See Pet. App. 3a-4a. The veil-piercing action, by contrast, involved the question whether Tru-Tech and petitioner possess separate personalities.[4] No precedent of this Court justifies considering the veil-piercing action to be ancillary to the ERISA action.[5]

A fiduciary duty determination under ERISA and a veil-piercing determination not only are governed by different legal principles but also are highly fact-intensive. In assessing petitioner's fiduciary liability, the trial court looked at evidence of the business decisions made by Tru-Tech's officers and directors in establishing and administering the ERISA plan. The court expressly found that "[n]either D. Grant Peacock & Co. nor D. Grant Peacock exercised discretionary authority and control over the management and administration of the plan and disposition of its assets," and thus were not plan fiduciaries. *Thomas* v. *Tru-Tech*, No. 87-

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[4] In fact, the conduct that gave rise to the veil-piercing action arose primarily *after* the ERISA judgment had been entered. See Pet. App. 39a-41a; p. 24, *infra*.

[5] The conclusion that the veil-piercing action is not necessary to, or a part of, the underlying ERISA judgment is confirmed by *Mackey* v. *Lanier Collection Agency & Service*, 486 U.S. 825, 833 (1988), which held that "ERISA does not provide an enforcement mechanism for collecting judgments won" in actions brought against plans by either purported beneficiaries or general creditors.

2243-3, 1988 U.S. Dist. LEXIS 15929, *31-32 (D.S.C. Nov. 28, 1988).

In the veil-piercing action, the trial court looked at entirely different facts: evidence of moneys owed to and by Tru-Tech, transfers of notes and consideration paid therefor, and company accounting practices for periods before and after the original judgment. Pet. App. 40a-42a. This inquiry had virtually no overlap with the fiduciary duty inquiry. The factual interdependence between the two actions necessary to support ancillary jurisdiction is clearly lacking.

Rather than adopting an expansive view of federal jurisdiction to enforce judgments, this Court and the lower courts have generally asked whether the subsequent enforcement action arises from a common nucleus of operative facts with the underlying federal proceeding and therefore can be said to form part of the same constitutional case. See *Owen Equipment & Erection Co.* v. *Kroger*, 437 U.S. 365, 371 (1978); *United Mine Workers* v. *Gibbs*, 383 U.S. 715, 725 (1966). These courts have found that the requisite factual nexus is lacking when the plaintiff asserts unrelated, fact-specific, disputed claims, after the end of the principal litigation.[6]

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[6] See, *e.g.*, *Sandlin* v. *Corporate Interiors, Inc.*, 972 F.2d 1212, 1217 (10th Cir. 1992) ("when postjudgment proceedings seek to hold nonparties liable for a judgment on a theory that requires proof on facts and theories significantly different from those underlying the judgment, an independent basis for federal jurisdiction must exist"); *Berry*, 795 F.2d at 455 (finding that court lacked jurisdiction, in part, because original judgment arose from alleged constitutional violation and subsequent garnishment action arose from contract); *Redding Ford* v. *California State Board of Equalization*, 722 F.2d 496, 498 (9th Cir. 1983) ("ancillary jurisdiction cannot be extended beyond the claims asserted in one action"), cert. denied, 469 U.S. 817 (1984); *Manway Constr. Co.* v. *Housing Authority of Hartford*, 711 F.2d 501, 504 (11th Cir.

The Fourth Circuit should have followed the same approach. If it had, it would have been compelled to conclude that there is no common nucleus of fact between the issues raised in the ERISA action and the issues dispositive in the veil-piercing action. Thus, there is no basis to assert ancillary jurisdiction here.

II. PIERCING THE CORPORATE VEIL TO IMPOSE PERSONAL LIABILITY ON A NONFIDUCIARY IS INCONSISTENT WITH THE ERISA STATUTORY SCHEME

Respondent was awarded a judgment against Tru-Tech under ERISA. In the course of that litigation, Tru-Tech was held to be a fiduciary of an ERISA pension plan, and petitioner was held not to be a fiduciary. When Tru-Tech was unable to satisfy the judgment, respondent commenced this suit against petitioner, contending that ERISA contains an implied cause of action — corporate veil-piercing — that would make petitioner liable as if he were an ERISA fiduciary.

This theory of implied liability undercuts the explicit, carefully-crafted distinction in ERISA between the duties of those who are fiduciaries under the statute and those who are not. That distinction — unchanged since ERISA was enacted in 1974 — is fundamental in regulating the relationship between ERISA plans and those, such as the member firms of amicus curiae NAREIM, with whom the plans do business. These relationships have been guided for over 20 years by the definition of fiduciary status in ERISA. Particularly in view of this Court's unwillingness to infer causes of action under

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1983) (contempt action against garnishee bank raised state law claims, between non-diverse parties, and was "so far removed" from original contract action that ancillary jurisdiction could not be invoked).

ERISA (see *Mertens* v. *Hewitt Associates*, 113 S. Ct. 2063, 2067 (1993)), the decision below should be reversed.

A. ERISA Unambiguously Delineates Who Shall Bear The Burdens Of Fiduciary Responsibility

Congress devoted an entire subpart of ERISA to the subject of "Fiduciary Responsibility," §§ 401-414, 29 U.S.C. §§ 1101-1114. The core subject of this regulation, a "fiduciary" to a plan, must comply with detailed obligations set forth in the statute. The duties and responsibilities of fiduciaries include "the proper management, administration, and investment of [plan] assets, the maintenance of proper records, the disclosure of specified information, and the avoidance of conflicts of interest." *Massachusetts Mut. Life Ins. Co.* v. *Russell*, 473 U.S. 134, 142-143 (1985). A fiduciary is "personally liable" for any breach of the "responsibilities, obligations, or duties imposed upon fiduciaries" by Title I, § 409(a), 29 U.S.C. § 1109(a). The fiduciary is also barred from causing the plan to engage in certain "prohibited transactions," § 406(a), 29 U.S.C. § 1106(a), and from engaging in other prohibited transactions involving self-dealing or conflict of interest. See § 406(b), 29 U.S.C. § 1106(b). Several remedial provisions provide broad rights of action to both private parties and the Secretary of Labor against errant plan fiduciaries. See, *e.g.*, § 502, 29 U.S.C. §§ 1132.

The statute succinctly provides three ways to become an ERISA fiduciary. First, the plan instrument must provide for at least one "named fiduciary." See § 402(a), 29 U.S.C. § 1102(a). Second, the plan instrument may authorize named fiduciaries to designate other persons to carry out certain fiduciary responsibilities under the plan. See § 405(c)(1)(B), 29 U.S.C. § 1105(c)(1)(B). Persons so designated are deemed to be fiduciaries under ERISA. See § 3(21)(A), 29 U.S.C. § 1002(21)(A).

Third, and most broadly, ERISA contains a functional definition of fiduciary status. See § 3(21)(A), 29 U.S.C. § 1002(21)(A). Even if a corporation or an individual is not named or specifically designated as a fiduciary, that corporation or individual functionally will take on fiduciary status:

> to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.

§ 3(21), 29 U.S.C. § 1002(21). By defining ERISA fiduciaries functionally, Congress "expand[ed] the universe of persons subject to fiduciary duties — and to damages — under section 409 [29 U.S.C. § 1109]." *Mertens*, 113 S. Ct. at 2071.

This broad functional definition of fiduciary status cuts through the labels in corporate structures. For example, members of a board of directors of a corporation are treated as fiduciaries to the extent that their activities fall within Section 3(21). See 29 C.F.R. § 2509.75-8, D-4 (1994); *Martin* v. *Harline*, 15 E.B.C. (BNA) 1138 (D. Utah 1992); *Newton* v. *Van Otterloo*, 756 F. Supp. 1121, 1132 (N.D. Ind. 1991). Indeed, an officer of a corporation that is a named fiduciary of a plan may, in acting for the corporation, also be regarded as a fiduciary individually. Compare *Confer* v. *Custom Eng'g Co.*, 952 F.2d 34 (3d Cir. 1991) (corporate officer not a fiduciary individually), with *Kayes* v. *Pacific Lumber Co.*, 51 F.3d 1449 (9th Cir. 1995) (corporate officer who acts in a fiduciary capacity may be held liable individually as a fiduciary).

ERISA's distinction between fiduciary and nonfiduciary status is the essential guide for parties dealing with pension plans, such as the members of NAREIM. For example, an investment firm may be appointed by a named fiduciary to serve as an "investment manager" of the assets of the plan. See § 402(c)(3), 29 U.S.C. § 1102(c)(3). An investment manager under ERISA is a fiduciary with power over plan assets, which is registered as an investment advisor under the Investment Advisers Act of 1940, or is a bank or insurance company, and which has acknowledged in writing its fiduciary status. See § 3(38), 29 U.S.C. § 1002(38). Due to the functional definition of a fiduciary under ERISA, however, the possible extent of fiduciary status is not limited to the corporate entity appointed investment manager. Thus, other corporate entities, individuals affiliated with the investment manager, and even the shareholders are charged under ERISA with knowing that if they act as fiduciaries, they must both meet the obligations of and be subject to liability as fiduciaries.

The practical implications of the distinction between fiduciary and nonfiduciary status are substantial. For example, in an investment relationship that is not governed by ERISA, the parties may define the standard of care by contract and agree to exculpation (on a showing of good faith, or absent proof of negligence) as to the performance of the investment. Under ERISA, however, an investment manager is held to a very high statutory standard of care, § 404(a)(1), 29 U.S.C. § 1104(a)(1), which cannot be varied by the parties, and exculpation of an investment manager is void as against public policy. § 410(a), 29 U.S.C. § 1110(a); see *Kayes*, 51 F.3d at 1460.

Furthermore, even if the investment manager's conduct satisfies ERISA's standard of care generally, under ERISA the investment manager still must comply with the statute's highly detailed prohibited transaction rules (§ 406(a), 29 U.S.C. § 1106(a)), which bar fiduciaries from causing the

plan to enter into investments that directly or indirectly involve parties in interest.[7] In addition, a fiduciary may be liable for breaches committed by cofiduciaries. Implementing procedures to comply with ERISA's stringent rules and purchasing fiduciary liability insurance to protect against inadvertent violations of ERISA increase the operating costs of investment managers. Thus, there are very tangible reasons for investment managers, and the corporations and individuals related to them, to understand precisely when they are deemed to be fiduciaries subject to fiduciary liability under ERISA and when they are not.

Until now, that guidance has been provided by the clear statutory language of ERISA and by more than 20 years of interpretation of that language by the Department of Labor and the courts. The decision below would introduce massive confusion by imposing liabilities on nonfiduciaries that are equivalent to those that fiduciaries have assumed expressly.

B. ERISA's Fiduciary-Nonfiduciary Distinction Would Be Rendered Meaningless By Inferring A Cause Of Action For Veil-Piercing To Reach Nonfiduciaries

Respondent brought this suit under ERISA to require petitioner, a nonfiduciary, to satisfy a judgment rendered against Tru-Tech, a fiduciary. Respondent did not premise his claims against petitioner on a theory that sought equitable relief, under § 502(a)(3), 29 U.S.C. § 1132(a)(3), against a nonfiduciary for knowing participation in a fiduciary breach.

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[7] A very recent prohibited transaction exemption proposed by the Department of Labor illustrates the complexity of administering the investment activities of pension plans in compliance with the prohibited transaction rules. The Labor Department noted, as part of the grounds for proposing the retroactive exemption, that the General Motors plans currently have 1,375 entities that are parties in interest with respect to the plans. 60 Fed. Reg. 33,861, 33,863 (June 29, 1995).

Thus, the viability of such an action under Section 502(a)(3), a question that this Court reserved in *Mertens*, 113 S. Ct. at 2067-2068, is not directly presented here. Instead, the Fourth Circuit devised a federal common law rule of liability with no specific foundation in ERISA. This Court has stated a strong presumption against inferring new causes of action or remedies within ERISA. *Russell*, 473 U.S. at 146-148; *Mertens*, 113 S. Ct. at 2067. The Court should be particularly reluctant to infer liability against the nonfiduciary here, where the result would undercut ERISA's fundamental distinction between fiduciaries and nonfiduciaries.

1. The Fourth Circuit's Reasoning Lacks Support in the Statute

The Fourth Circuit did not attempt to locate a specific relevant source of nonfiduciary duty in ERISA or a cause of action in the language of the statute. Rather, the court of appeals appears to have relied entirely on ERISA's general purpose of protecting employee benefits as the basis for a new common law rule imposing liability on nonfiduciaries. Under ERISA, however, "vague notions of a statute's 'basic purpose' are * * * inadequate to overcome the words of its text regarding the specific issue under consideration." *Mertens*, 113 S. Ct. at 2071.

The Fourth Circuit did not explicitly acknowledge that it was sanctioning the imposition of fiduciary liability on a nonfiduciary. As a result, the court of appeals did not address the open issue, post-*Mertens*, of the liability of a nonfiduciary under Section 502(a)(3) of ERISA for knowing participation in a fiduciary breach. Accordingly, the court below avoided a confrontation with the post-*Mertens* decisions in three other circuits that have decided against such knowing participation liability of a nonfiduciary. See *Reich* v. *Rowe*, 20 F.3d 25 (1st Cir. 1994) (nonfiduciary accounting service provider); *Reich* v. *Continental Casualty Co.*, 33 F.3d 754, 757 (7th Cir. 1994), cert. denied, 115 S. Ct. 1104 (1995) (nonfiduciary provider of fiduciary liability insurance policy);

Reich v. *Compton*, No. 93-2019, 1995 WL 329911 (3d Cir. June 5, 1995) (nonfiduciary lessee); see also *Buckley Dement, Inc.* v. *Travelers Plan Administrators of Illinois, Inc.*, 39 F.3d 784, 789 (7th Cir. 1994) (nonfiduciary claims administrator).

Instead, the Fourth Circuit relied upon "a liberal veil-piercing standard" (Pet. App. 23a), which the First Circuit had fashioned in *Alman* v. *Danin*, 801 F.2d 1 (1st Cir. 1986), to require the controlling shareholders of an employer to satisfy the corporation's contractual obligation under a collective bargaining agreement to contribute to multi-employer benefit plans. The duty of an employer to contribute to a multi-employer plan pursuant to a collective bargaining agreement is a statutory obligation of the employer under ERISA. § 515, 29 U.S.C. § 1145. But the employer takes on no greater duty under ERISA than it has assumed contractually in bargaining to contribute to the multi-employer plan. In contrast, a corporate fiduciary takes on specific statutory duties of care, solely because of the corporation's status as a fiduciary under ERISA. Given these distinctions under the structure of ERISA, it was plainly inappropriate to follow *Alman* and import veil-piercing notions here.

2. Without More, This Court Should Not Infer a New Cause of Action from ERISA

There is a strong presumption against federal courts creating new causes of action or remedies within ERISA. *Mertens*, 113 S. Ct. at 2067. "The presumption that a remedy was deliberately omitted from a statute is strongest when Congress has enacted a comprehensive legislative scheme including an integrated system of procedures for enforcement." *Russell*, 473 U.S. at 147 (quoting *Northwest Airlines, Inc.* v. *Transport Workers*, 451 U.S. 77, 97 (1981)). There is no doubt that ERISA is the prototypical "comprehensive and reticulated" statute. *Mertens*, 113 S. Ct. at 2066 (quoting *Nachman Corp.* v. *PBGC*, 446 U.S. 359,

361 (1980)).[8] As much as the Fourth Circuit struggled (for jurisdictional reasons) to characterize the action against petitioner as simply piggybacking on an underlying ERISA claim (Pet. App. 12a), the reality is that the creation of a new veil-piercing cause of action runs afoul of the presumption that Congress deliberately omitted the cause of action in the first place, without offering any justification for doing so.

There are very strong reasons not to buck this presumption. First, ERISA is the result of a delicate balancing of competing interests by Congress. Although the purpose of ERISA is to protect the security of employees, Congress had to engage in "certain cost-benefit analyses * * * in order to fashion a comprehensive regulatory scheme." *Rowe*, 20 F.3d at 32. One key legislative decision was to define carefully the obligations, and the causes of action to enforce those obligations, associated with "increasing the number of fiduciary parties and the scope of fiduciary responsibility." *Id.* at 32-33. This was Congress' chosen method of "containing pension costs," *Mertens*, 113 S. Ct. at 2072, and meeting the stated objective of preserving "the soundness and stability of plans with respect to adequate funds to pay promised benefits." § 2(a), 29 U.S.C. § 1001(a). Allowing an implied cause of action vitiating ERISA's fundamental distinctions between fiduciaries and nonfiduciaries would upset the balance crafted by Congress.

Second, the costs associated with such a substantial expansion of ERISA-based liability are great. As one pension

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[8] The remaining components of the statutory scheme are tightly woven: "carefully integrated" civil enforcement provisions, § 502, 29 U.S.C. § 1132; *Russell*, 473 U.S. at 146; "clearly expansive" preemptive powers, § 514, 29 U.S.C. § 1144; *New York State Conference of the Blue Cross & Blue Shield Plans* v. *Travelers Insurance Company*, 115 S. Ct. 1671, 1677 (1995); and a complex regulatory system in Title IV governing plan terminations.

expert told the Senate Finance Committee's Subcommittee on Pension Plans during the consideration of ERISA:

> Unless this system [of liability for breaches of fiduciary duty] is developed with the utmost care, fiduciaries will avoid exercising initiative, judgment, individual responsibility, or similar subjective attention to individual plan management. The essential element of the private system — flexibility — will be compromised. Undue conservatism will be encouraged — to the detriment of the employees, the employer, and the economy as a whole.

Private Pension Plan Reform: Hearings Before the Subcommittee on Private Pension Plans of the Senate Comm. on Finance, 93rd CONG., 1ST SESS. 671-672 (1973) (statement of John S. Nolan).

Unfortunately, the Fourth Circuit ignored this warning. Rather than grapple with the language of the statute, the court of appeals heaped a daunting expansion of common law liability atop the shaky base of the general protective purposes of the statute. But as the Ninth Circuit observed in criticizing similar attempts under ERISA in the pre-*Mertens* era, they "have built very much on very little." *Nieto* v. *Ecker*, 845 F.2d 868, 872 (9th Cir. 1988). See also *Rodriguez* v. *United States*, 480 U.S. 522, 526 (1987) (rejecting the vice of "simplistically * * * assum[ing] that whatever furthers the statute's primary objective must be the law"). Such a practice makes ERISA liabilities wholly unpredictable, and the numerous industries that rely upon a clear understanding of the statute require a more stable legal environment in which to operate. To be sure, Congress intended the federal courts to have the power to develop a common law of ERISA, at least interstitially, see *Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. 101, 110 (1989), but the courts should "incorporate a given trust law principle [only] if the statute's text negates an inference that the principle was omitted deliberately from the statute." *Useden* v. *Acker*, 947

F.2d 1563, 1581 (11th Cir. 1991); accord *Rowe*, 20 F.3d at 32.

Third, ERISA already contains many provisions in which Congress explicitly disregarded the corporate form in order to further the statutory purposes. In addition to the functional definition of fiduciary, the highly technical rules applicable to transactions with parties in interest (§ 3(14), 29 U.S.C. § 1002(14)) determine whether transactions with shareholders of fiduciaries are, or are not, prohibited. § 406(a), 29 U.S.C § 1106(a). Congress also concluded that certain provisions of part 2 of Title I of ERISA, establishing minimum participation, vesting and benefit accrual standards, should be applied as if all corporations and all trades or businesses under common control were a single employer. §§ 210(c), (d), 29 U.S.C. §§ 1060(c), (d). Similarly, Congress chose to disregard the corporate form in certain funding provisions of part 3 of Title I of ERISA, specifically providing joint and several liability on all members of a controlled group of trades or businesses for funding obligations (§ 302(c)(11)(B), 29 U.S.C. § 1082(c)(11)); imposing a lien for failure to fund on the property of all members of such a controlled group (§ 302(f), 29 U.S.C. § 1082(f)); and considering the financial condition of all members of such a controlled group for purposes of providing variances from the minimum funding requirements for substantial business hardships (§ 303(d)(2), 29 U.S.C. § 1083(d)(2)).[9] The detailed attention that

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[9] Title II of ERISA amended the Internal Revenue Code to incorporate many of the substantive provisions of Title I of ERISA. Sections 414(b) and 414(c) of the Code impose controlled group principles for selected provisions relating to certain tax qualified employee benefit plans. 26 U.S.C. §§ 414(b)-414(c). Certain provisions in Title IV of ERISA similarly apply specifically to all trades or businesses under common control, including the obligation to pay premiums to the Pension Benefit Guaranty Corporation (§ 4007(e)(2), 29 U.S.C. § 1307(e)(2)); the ability to engage in a

Congress gave to recognizing or disregarding the corporate form throughout ERISA belies the conclusion that Congress intended the courts to devise a liberal veil-piercing standard of general applicability.

Imposing liability on a nonfiduciary controlling shareholder also would produce, in practice, a contorted result that is inconsistent with the structure of ERISA. The trustees must have "exclusive authority and discretion to manage and control the assets of the plan." § 403(a), 29 U.S.C. § 1103(a). However, the trust may delegate to an asset manager the authority to manage, acquire or dispose of plan assets. § 403(a)(2), 29 U.S.C. § 1103(a)(2). If this authority is delegated to an investment manager, the controlling shareholder of the investment manager takes on fiduciary duties and fiduciary liability only if he agrees to become a fiduciary or acts in fact as a fiduciary. But, if the "liberal veil-piercing standard" of the Fourth Circuit is adopted (Pet. App. 23a), the controlling shareholder may be subject to veil-piercing liability even if he has been careful to refrain from acting as a fiduciary, due to his nonfiduciary conduct of the business of the corporation. Thus, controlling shareholders, confronted with the threat of liability under a liberal veil-piercing standard, perversely may be able to protect themselves against liability under ERISA only by becoming more deeply involved in the corporation's fiduciary activities. Whether the controlling shareholder is capable of performing as a skilled fiduciary becomes less relevant than responding to this imperative. The carefully articulated delegation of authority permitted under ERISA thus may become skewed by

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distress termination under § 4041(c)(2), 29 U.S.C. § 1341(c)(2); reportable events under § 4043(a), 29 U.S.C. § 1343(a); liability with respect to plan terminations and withdrawals, §§ 4062-4064, 29 U.S.C. §§ 1362-1364; and the lien imposed by § 4068, 29 U.S.C. § 1368.

the foreign pressures of defending against veil-piercing liability.

C. Veil-Piercing To Impose Liability On A Nonfiduciary Is Inconsistent With ERISA's Functional Definition Of A Fiduciary

The functional definition of a fiduciary in Section 3(21) of ERISA is an explicit and dynamic statutory mechanism for attributing fiduciary responsibility to the true, behind-the-scenes wielders of power over a plan. It is therefore protective: if the "named" fiduciary really is acting as a fiduciary in name only, the functional definition pins fiduciary duties — and thus personal liability — upon additional parties. In this way, the functional definition functions very much like the common law doctrine of veil-piercing, placing substance over form.

However, veil-piercing analysis differs from the functional ERISA analysis in such a way that it would be anomalous to use veil-piercing to impose fiduciary liability on an individual (such as petitioner) who has already been found to be a nonfiduciary under ERISA. Though procedurally similar, the two analyses differ in substance. Veil-piercing is a traditional state-law method of assigning substantive liability against a person or entity when that person or entity exercises such complete control over a corporation that the corporate form is adjudged to be a sham. See Pet. App. 11a. By contrast, the analysis required by ERISA looks beyond issues of general corporate control to the particular type of control specified in Section 3(21) as triggering fiduciary duties. This factual link to plan assets and affairs is essential to describing an ERISA cause of action, because fiduciary duties and obligations make sense only in terms of their relation to a plan.[10] In other words, it makes perfect sense to have situa-

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[10] That is why the factors analyzed in veil-piercing cannot generate ERISA liability; they are all cast in reference to *corporate*,

tions in which a shareholder would be considered a fiduciary under ERISA even though it would be inappropriate to pierce the corporate veil to impose other corporate liabilities. But it confuses the purposes of the statute and compromises its integrity to employ veil-piercing to impose personal liability on a controlling shareholder — who, by virtue of his behavior, has *not* triggered any fiduciary duties and obligations — and to call that liability ERISA liability.

The Fourth Circuit considered the argument that veil-piercing should not be substituted for ERISA's functional fiduciary analysis but dismissed it in a short footnote. See Pet. App. 19a n.14. The court of appeals observed that "[t]he tests for ERISA fiduciary liability and veil-piercing are not identical," and it stressed that "most of the activity leading to the conclusion of veil-piercing occur[red] *after* the activity pursuant to which the corporation [was] deemed to have breached its ERISA fiduciary duties." *Ibid.* But this statement hardly explains why it is appropriate to superimpose a court-made veil-piercing theory on top of the fiduciary analysis adopted by Congress, much less why ERISA's functional analysis could not simply have been applied to the changed factual picture that existed at the time of the enforcement action. Simply stated, the relevant status under ERISA is that of a fiduciary, and liability should follow only if a person is named or functions as a fiduciary.

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not plan, affairs — *e.g.*, undercapitalization of the corporation, failure to observe corporate formalities, siphoning of the corporation's funds by the dominant shareholder, non-functioning of corporate officers and directors, and commingling of personal and corporate assets. See generally 1 William M. Fletcher, Fletcher Cyclopedia of the Law of Corporations § 41.30 (perm. ed. rev. vol. 1990).

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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